

(h) *Special rules for partners and S corporation shareholders*—(1) *In general.* Under section 179(d)(8) and § 1.179-2(c), a partner may have a carryover of disallowed deduction with respect to the cost of section 179 property elected to be expensed by the partnership and allocated to the partner. A partner who is allocated section 179 expenses from a partnership must reduce the basis of his or her partnership interest by the full amount allocated regardless of whether the partner may deduct for the taxable year the allocated section 179 expenses or is required to carry forward all or a portion of the expenses. Similar rules apply to S corporation shareholders.

(2) *Dispositions and other transfers of a partner's interest in a partnership or a shareholder's interest in an S corporation.* A partner who disposes of a partnership interest, or transfers a partnership interest in a transaction in which gain or loss is not recognized in whole or in part (including transfers of a partnership interest at death), may have an outstanding carryover of disallowed deduction of section 179 expenses allocated from the partnership. In such a case, immediately before the transfer the partner's basis in the partnership interest is increased by the amount of the partner's outstanding carryover of disallowed deduction with respect to the partnership interest. This carryover of disallowed deduction is not available as a deduction to the transferor or transferee partner of the section 179 property. Similar rules apply to S corporation shareholders.

(3) *Examples.* The following examples illustrate the provisions of this paragraph (h).

Example 1. (i) G is a general partner in GD, a calendar-year partnership, and is engaged in the active conduct of GD's business. During 1991, GD purchases and places section 179 property in service and elects to expense a portion of the cost of the property under section 179. GD allocates \$2,500 of section 179 expenses and \$15,000 of taxable income (determined without regard to the section 179 deduction) to G. The income was derived from the active conduct by GD of a trade or business.

(ii) In addition to being a partner in GD, G conducts a business as a sole proprietor. During 1991, G purchases and places in service office equipment costing \$25,000 and a computer costing \$10,000 in connection with the

sole proprietorship. G elects under section 179(c) and § 1.179-5 to expense \$7,500 of the cost of the office equipment. G has a taxable loss (determined without regard to the section 179 deduction) derived from the active conduct of this business of \$12,500.

(iii) G has no other taxable income (or loss) derived from the active conduct of a trade or business during 1991. G's taxable income limitation for 1991 is \$2,500 (\$15,000 taxable income allocated from GD less \$12,500 taxable loss from the sole proprietorship). Therefore, G may deduct during 1991 only \$2,500 of the \$10,000 of section 179 expenses. G notes on the appropriate books and records that G expenses the \$2,500 of section 179 expenses allocated from GD and carries forward the \$7,500 of section 179 expenses with respect to the office equipment purchased by G's sole proprietorship.

(iv) On January 1, 1992, G sells the office equipment G's sole proprietorship purchased and placed in service in 1991. Under paragraph (f) of this section, immediately before the sale G increases the adjusted basis of the office equipment by \$7,500, the amount of the outstanding carryover of disallowed deduction with respect to the office equipment.

Example 2. (i) Assume the same facts as in *Example 1*, except that G notes on the appropriate books and records that G expenses \$2,500 of section 179 expenses relating to G's sole proprietorship and carries forward the remaining \$5,000 of section 179 expenses relating to G's sole proprietorship and \$2,500 of section 179 expenses allocated from GD.

(ii) On January 1, 1992, G sells G's partnership interest to A. Under paragraph (h)(2) of this section, immediately before the sale G increases the adjusted basis of G's partnership interest by \$2,500, the amount of the outstanding carryover of disallowed deduction with respect to the partnership interest.

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§ 1.179-4 Definitions.

The following definitions apply for purposes of section 179 and §§ 1.179-1 through 1.179-6:

(a) [Reserved] For further guidance, see § 1.179-4T(a).

(b) *Section 38 property.* The term *section 38 property* shall have the same meaning assigned to it in section 48(a) and the regulations thereunder.

(c) *Purchase.* (1)(i) Except as otherwise provided in paragraph (d)(2) of this section, the term *purchase* means any acquisition of the property, but only if all the requirements of paragraphs (c)(1)(ii), (iii), and (iv) of this section are satisfied.

(ii) Property is not acquired by purchase if it is acquired from a person

whose relationship to the person acquiring it would result in the disallowance of losses under section 267 or 707(b). The property is considered not acquired by purchase only to the extent that losses would be disallowed under section 267 or 707(b). Thus, for example, if property is purchased by a husband and wife jointly from the husband's father, the property will be treated as not acquired by purchase only to the extent of the husband's interest in the property. However, in applying the rules of section 267 (b) and (c) for this purpose, section 267(c)(4) shall be treated as providing that the family of an individual will include only his spouse, ancestors, and lineal descendants. For example, a purchase of property from a corporation by a taxpayer who owns, directly or indirectly, more than 50 percent in value of the outstanding stock of such corporation does not qualify as a purchase under section 179(d)(2); nor does the purchase of property by a husband from his wife. However, the purchase of section 179 property by a taxpayer from his brother or sister does qualify as a purchase for purposes of section 179(d)(2).

(iii) The property is not acquired by purchase if acquired from a component member of a controlled group of corporations (as defined in paragraph (g) of this section) by another component member of the same group.

(iv) The property is not acquired by purchase if the basis of the property in the hands of the person acquiring it is determined in whole or in part by reference to the adjusted basis of such property in the hands of the person from whom acquired, or is determined under section 1014(a), relating to property acquired from a decedent. For example, property acquired by gift or bequest does not qualify as property acquired by purchase for purposes of section 179(d)(2); nor does property received in a corporate distribution the basis of which is determined under section 301(d)(2)(B), property acquired by a corporation in a transaction to which section 351 applies, property acquired by a partnership through contribution (section 723), or property received in a partnership distribution which has a carryover basis under section 732(a)(1).

(2) Property deemed to have been acquired by a new target corporation as a result of a section 338 election (relating to certain stock purchases treated as asset acquisitions) will be considered acquired by purchase.

(d) *Cost.* The cost of section 179 property does not include so much of the basis of such property as is determined by reference to the basis of other property held at any time by the taxpayer. For example, X Corporation purchases a new drill press costing \$10,000 in November 1984 which qualifies as section 179 property, and is granted a trade-in allowance of \$2,000 on its old drill press. The old drill press had a basis of \$1,200. Under the provisions of sections 1012 and 1031(d), the basis of the new drill press is \$9,200 (\$1,200 basis of old drill press plus cash expended of \$8,000). However, only \$8,000 of the basis of the new drill press qualifies as cost for purposes of the section 179 expense deduction; the remaining \$1,200 is not part of the cost because it is determined by reference to the basis of the old drill press.

(e) *Placed in service.* The term *placed in service* means the time that property is first placed by the taxpayer in a condition or state of readiness and availability for a specifically assigned function, whether for use in a trade or business, for the production of income, in a tax-exempt activity, or in a personal activity. See § 1.46-3(d)(2) for examples regarding when property shall be considered in a condition or state of readiness and availability for a specifically assigned function.

(f) *Controlled group of corporations and component member of controlled group.* The terms *controlled group of corporations* and *component member* of a controlled group of corporations shall have the same meaning assigned to those terms in section 1563 (a) and (b), except that the phrase "more than 50 percent" shall be substituted for the phrase "at least 80 percent" each place it appears in section 1563(a)(1).

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